

**COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION**

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**In the Matter of:**

**INVESTIGATION INTO THE )  
MEMBERSHIP OF LOUISVILLE )  
GAS AND ELECTRIC )  
AND KENTUCKY UTILITIES )  
COMPANY IN THE MIDWEST )  
INDEPENDENT TRANSMISSION )  
SYSTEM OPERATOR, INC )**

**CASE NO. 2003-00266**

**POST HEARING BRIEF OF THE ATTORNEY GENERAL**

On July 17, 2003, the Commission opened an investigation to determine whether Louisville Gas and Electric Company ("LG&E") and Kentucky Utilities Company ("KU") receive benefits from the services provided by the Midwest Independent System Operator ("MISO") commensurate with the costs. LG&E and KU (collectively the "Companies") present testimony indicating that withdrawal from MISO and operation on a stand-alone basis would be more advantageous to the Companies than would continued MISO membership. Because the Federal Energy Regulatory Commission ("FERC") would have to grant authority to withdraw, the Companies ask the Commission to direct them to seek authority from FERC to withdraw from MISO. The Companies also ask the Commission to allow them to recover both the costs of the withdrawal, should authority to withdraw be granted by the FERC, and the ongoing costs of MISO participation until they withdraw. MISO presented testimony to demonstrate the benefits of participation in MISO for KU and LG&E. The Attorney General ("AG") and the Kentucky Industrial Utility Customers ("KIUC") participated in the proceeding but did not present testimony.

**LG&E AND KU SHOULD BE ENCOURAGED TO SEEK APPROVAL TO WITHDRAW FROM MISO.**

Because the role of independent transmission operators and regional control of transmission assets is very much an evolving concept, LG&E and KU have found themselves participants in and paying for an entity different from that which they joined and that which might provide cost-effective benefits for the Companies. MISO is expanding its role beyond that which it was to hold when the Companies were involved in the process of creating and joining MISO. The areas of expanded activity and the costs for those activities do not appear to be cost justified for LG&E and KU. Further, the impetus toward and drive for a nationally deregulated/competitive electric industry has slowed significantly, particularly in Kentucky, from that which was present when the Commission encouraged LG&E and KU to join an independent system operator.<sup>1</sup>

Absent a competitive market and in the presence of continued strong regulation, there is little reason for LG&E and KU to participate in a regional transmission organization. Reliability is the main factor established as the reason low-cost providers should participate in a regional transmission organization. LG&E and KU had good track records for reliability before joining MISO.<sup>2</sup> There is no reason to believe that they are not capable of again maintaining a good reliability record under similar circumstances. MISO contends that the Companies' track records are irrelevant in today's circumstances and pose the question of whether the function of providing reliable transmission is the

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<sup>1</sup> See, Case No. 2000-095, *Joint Application of Powergen plc., LG&E Energy Corp., Louisville Gas and Electric Company and Kentucky Utilities Company for approval of Merger*, and Case No. 2001-104, *Joint Application for the Transfer of Louisville Gas and Electric Company and Kentucky Utilities Company in Accordance with E.ON AG's Planned Acquisition of Powergen plc.*

<sup>2</sup> MISO was able to establish only that there **may** have been near misses in reliability, not that there were any actual failures of reliability for LG&E and KU.

same in today's circumstances as it was before the Companies joined MISO, and thus, whether similar efforts by the Companies at similar costs can be effective to provide the needed reliability. Despite the efforts of MISO and the Companies, that question continues to be unanswered.

From the consumer's perspective, this is a time of flux in which no one appears to have definitive answers. It is a time when there has been no loss of reliability in Kentucky when the Companies' transmission systems were operated by the Companies and when they were operated by MISO, but MISO has had an unfortunate role in the August 2003 blackout. It is a time when the labor costs attendant to the Companies' transmissions operations have not gone down significantly despite the fact that they have transferred functional control of the transmission assets to MISO and have added a layer of MISO-related transmission costs - costs that will continue to escalate if they continue to be members of MISO. Absent the ability to clearly determine that a gain in reliability is obtained in return for the added cost of participation in MISO, there appears to be no good reason to continue to participate in MISO.

Only if the Companies seek to leave MISO can the actual exit cost be determined. Only if the Companies seek to leave MISO can it be determined whether they can obtain needed services in some other contractual fashion from MISO or others. Only if they seek to leave MISO will the Companies be able to determine whether the FERC will permit stand-alone operations for these Companies whose primary purpose continues to be to serve native load in a fully regulated service territory. Though the Companies and MISO have given the most educated guesses possible, neither has been able to provide the information that will be gained only from the process of the effort to exit MISO.

Therefore, absent the making of a strong case for continued participation in MISO – a case that was not made in this proceeding - the Commission should authorize the Companies to seek an exit from MISO.

**FOR RATEMAKING PURPOSES, IF AN EXIT FROM MISO IS AUTHORIZED AND AN EXIT FEE IS IMPOSED, THE COMMISSION SHOULD REQUIRE THE COMPANIES TO ESTABLISH AN OFF-SETTING REGULATORY ASSET AND LIABILITY TO BALANCE ANY EXIT FEE AGAINST THE CONTINUING LEVELS OF SCHEDULE 10 EXPENSES BUILT INTO THE BASE RATES IN CURRENTLY PENDING RATE CASES.**

KU and LG&E have sought recovery of MISO Schedule 10 costs in their current rate cases.<sup>3</sup> At page 10-11 of his direct testimony, Mr. Beer has indicated the Companies' intent to continue to seek any ongoing MISO-related expenses as reflected in the test period as well as all *pro forma* adjustments in any base rate case pending receipt of final FERC approval to exit MISO. In this case, the Companies' seek approval to establish a regulatory asset for the MISO exit fee. As proposed by the Companies, a subsequent filing would be made to remove the MISO-related expenses from base rates and to begin amortization and base rate recovery of the regulatory asset over a specific term when the exit is granted. While the effort to be fair to the Companies and the customers in terms of cost recovery is apparent in the proposal's attempt to avoid concurrent recovery of both the built in level of MISO-related expenses and the regulatory asset comprised of the exit fee, the request sets up an invitation to single issue rate-making that is unwarranted and unnecessary.

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<sup>3</sup> Case No. 2003-00434 and Case No. 2003-00433, respectively.

If the Commission grants the request to establish a regulatory asset for the MISO exit fee, it should simultaneously establish an off-setting regulatory liability to be funded by the amount of MISO-related expenses that are built into the base rates established as a consequence of the currently pending rate cases (or any successor rate cases in which MISO-related expenses are authorized). The regulatory liability would be funded at the level of MISO-related expense built into the base rates commencing when the regulatory asset for the exit fees comes into being until the next rate case is filed, with an annual offset of the regulatory asset in the amount of the approved MISO-related expenses. At the time of the next rate case, if any portion of the regulatory asset remains unmet by the annual contribution of the off-setting regulatory liability, then an appropriate expense and amortization could be set up in the next base rate case to collect the remainder of the regulatory asset in the base rates established in that case. If another extended period of time were to pass before the Companies were to seek another rate increase such that the MISO-related expenses incorporated into rate base fully offset the regulatory asset in the interim and continued to increase the regulatory liability over and above the amount of the regulatory asset, any net remainder of that regulatory liability could be established as an appropriately amortized offset to the then requested increase in base rates. This proposal would treat the Companies and the ratepayers fairly and the Commission would not be forced into another instance of single issue rate-making. With this process, administrative efficiency would be promoted and the Commission would be acting within the clear bounds of its authority.

Respectfully Submitted,

GREGORY D. STUMBO  
ATTORNEY GENERAL



Elizabeth E. Blackford  
Assistant Attorney General

Certificate of Service and Notice of Filing

I hereby give notice that I have filed the original and ten true copies of the foregoing Post Hearing Brief of the Attorney General with the Executive Director of the Kentucky Public Service Commission, 211 Sower Boulevard, Frankfort, Kentucky and that I have served the parties of record by mailing a postage prepaid copy of same this the 26<sup>th</sup> day of April, 2004 to the following:

MICHAEL S BEER  
VP RATES & REGULATORY  
LOUISVILLE GAS & ELECTRIC CO.  
P O BOX 32010  
LOUISVILLE KY 40232-2010

MICHAEL L KURTZ ESQ  
BOEHM KURTZ & LOWRY  
36 EAST SEVENTH STREET SUITE 2110  
CINCINNATI OH 45202

STEPHEN G KOZEY ESQ  
MIDWEST ISO  
701 CITY CENTER DRIVE  
CARMEL IN 46032

KATHERINE K YUNKER ESQ  
YUNKER & ASSOCIATES  
P O BOX 21784  
LEXINGTON KY 40522-1784

KENDRICK R RIGGS ESQ  
OGDEN NEWELL & WELCH PLLC  
1700 CITIZENS PLAZA  
500 WEST JEFFERSON STREET  
LOUISVILLE KY 40202



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